

Exhibit No.:
Issues: Labor and Labor Related Expenses,
Support Services, Production Costs, and
Other Operating Expense,
Witness: Nikole L. Bowen
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Sponsoring Party: Missouri-American Water Company
Case No.: WR-2017-0285
SR-2017-0286
Date: June 30, 2017

MISSOURI PUBLIC SERVICE COMMISSION

**CASE NO. WR-2017-0285
CASE NO. SR-2017-0286**

DIRECT TESTIMONY

OF

NIKOLE L. BOWEN

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

Exhibit No. 5
Date 3/18/18 MR
File No. WR-2017-0285

Exhibit 5
WR-2017-0285
Direct Testimony of Nikole L. Bowen

**DIRECT TESTIMONY
NIKOLE L. BOWEN
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WR-2017-0285
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TABLE OF CONTENTS

I.	Introduction.....	2
II.	Labor and Labor Related Expenses.....	5
	A. Salaries and Wages	7
	B. Payroll Tax.....	8
	C. Group Insurance	9
	D. Employee Benefits	10
III.	Support Services.....	12
IV.	Production Costs	14
	A. Fuel and Power.....	14
	C. Chemicals.....	15
	D. Waste Disposal.....	16
	E. Purchased Water	16
V.	Other Operating Expenses.....	17
	A. Rents.....	17
	B. Transportation.....	18
	C. Postage & Customer Accounting.....	18
	D. Miscellaneous Expense	19
	E. Contract Services	19
	F. Maintenance Supplies & Services	20
	G. Tank Painting	21
	G. Insurance Other than Group	22
	H. Uncollectible Expense	23
	I. PSC Assessment Fee	24

DIRECT TESTIMONY

NIKOLE L BOWEN

I. INTRODUCTION

1

2 **Q. Please state your name and business address.**

3 A. My name is Nikole L. Bowen, and my business address is 727 Craig Road, St. Louis,
4 MO, 63141.

5 **Q. By whom are you employed and in what capacity?**

6 A. I am Senior Manager of Regulatory Services for American Water Works Service
7 Company, Inc. ("Service Company"). Service Company is a wholly owned subsidiary
8 of American Water Works Company, Inc. ("American Water") that provides services
9 to Missouri-American Water Company ("MAWC", "Missouri-American" or
10 "Company") and its affiliates.

11 **Q. What are your responsibilities in this position?**

12 A. My duties consist of reviewing, preparing and assisting in regulatory filings and related
13 activities for all of the regulated subsidiaries of American Water. My responsibilities
14 and my team's responsibilities include the preparation of written testimony, exhibits
15 and work papers in support of rate applications and other regulatory filings as well as
16 responses to data requests for Missouri-American and its regulated utility affiliates.
17 My duties also include staying apprised of economic and regulatory developments and
18 conditions that may affect regulated water utilities, rates and regulatory policy analysis,

1 support and analysis, guidance and coordination of process improvement to support
2 continuous improvement of rates and regulatory processes and services, data
3 compilation and reporting, data and revenue analysis.

4 **Q. Please describe your educational background.**

5 A. I am a graduate of Fontbonne University in Missouri with a Bachelor of Business
6 Administration.

7 **Q. What has been your business experience?**

8 A. I began my career with American Water in 2002 at the Customer Service Center
9 (“CSC”) in Alton IL. In 2009, I was promoted to Billing Manager, responsible for all
10 facets of the revenue generation process, new business integration into the Customer
11 Service Center, rates implementation, and Sarbanes Oxley Compliance for billing
12 related controls. In March 2015, I joined Regulatory Services and currently hold the
13 position of Senior Manager of Regulatory Services.

14 **Q. Have you previously testified in regulatory proceedings?**

15 A. Yes. I have assisted in the preparation of rate cases and presented testimony to the
16 Missouri Public Service Commission, the Kentucky Public Service Commission, and
17 the Iowa Utilities Board.

18 **Q. Have you prepared, or caused to be prepared, exhibits in support of Missouri-
19 American’s general rate case?**

20 A. I have overseen preparation of exhibits and workpapers in support of this general rate
21 case for Missouri-American.

1 **Q. What is the purpose of your testimony in this proceeding?**

2 A. The purpose of my direct testimony is to support and explain the following Company
3 expense levels: labor and labor related, support services, production, and other
4 operating expenses.

5 **Q. What methodology did the Company use in in making its pro forma adjustments
6 to its historical expense levels in this case?**

7 A. We employed a Future Test Year –

8 In general, the historical test year expenses (12 months ended December 31, 2016) were
9 updated to include known and measurable changes, adjusted based on Company
10 experience, or adjusted based on an inflation factor annualized, through the 12 months
11 ending May 31, 2018 (the “current test year”). The Company then used a monthly
12 projection for the 12 months ended May 31, 2019 (the “future test year”) using known
13 and measurable changes, adjustments based on Company experience, or adjustments
14 based on an inflation factor.

15

16 In order to obtain representative levels of expenses that can vary, MAWC used a three-
17 year average of Company experience for pro forma expense adjustments to labor and
18 labor related, main break expense, chemical costs, and purchased water. To gauge cost
19 increases, MAWC used the average Gross Domestic Product Price Index forecast as
20 compiled by Blue Chip Economic Indicators. We applied inflation to the following pro
21 forma expense adjustment: non-PBOP insurance expense, fuel and power, chemicals
22 expense, rents, purchased water, transportation, postage, customer accounting, contract
23 services, maintenance supplies and services, and insurance other than group. This

1 forecast is a survey of a wide range of financial professionals, including bank, academic
2 and corporate forecasters. As of May 2017, the 2017 GDP Price Index is 2.0% and the
3 2018 GDP Price Index is 2.1%.¹

4 **Q. Can you provide an overview of the increased Company's O&M expense level?**

5 A. MAWC is seeking recovery of \$133 million in O&M expense for the future test year
6 ending May 31, 2019, which represents about a 2.0% percent annual increase over
7 historical expense levels. As Andrew Clarkson explains in his direct testimony, the
8 Company is seeking to enhance its maintenance activities, including plant maintenance,
9 valve operation, hydrant maintenance and flushing to sustain a cost effective level of
10 service for our customers over the long term. The initiative to enhance the Company's
11 enhanced maintenance activities, results in a pro forma expense increase of roughly 7.9
12 million dollars. Service Company costs are also projected to increase by \$694,000,
13 from \$30.23 million in 2106 to \$30.93 million in for the future test year ending May
14 31, 2019. These cost increases are offset, in part, by the Company's ongoing cost
15 control efforts, which kept costs approximately level from 2010 to the historical year.
16 The Company also is projecting a \$774,670 decrease in uncollectible expense from
17 2016 through the future test year.

18 **III. LABOR AND LABOR RELATED EXPENSES**

19 **Q. Please describe MAWC's labor and labor related expense.**

¹ The Consumer Price Index (CPI) and the gross domestic product (GDP) price index and implicit price deflator are measures of inflation in the U.S. economy. The CPI measures price changes in goods and services purchased out of pocket by urban consumers, whereas the GDP price index and implicit price deflator measure price changes in goods and services purchased by consumers, businesses, government, and foreigners, but not importers. Source: United States Bureau of Labor Statistic

1 A. There are three classifications of employees at MAWC: union hourly employees, non-
2 union hourly employees, and exempt employees. Union hourly employees receive base
3 pay, overtime pay, and in some cases shift pay. Non-union hourly employees receive
4 base pay, overtime pay, and are eligible for performance pay. Exempt employees
5 receive base pay and are eligible for performance pay. Therefore, total compensation
6 for each classification of employees includes fixed pay (base pay) and some form(s) of
7 variable pay (e.g., overtime, shift pay, or performance pay). Labor related expenses
8 include payroll tax, pension expense, postretirement benefits other than pension
9 (“PBOP”), group insurance, 401k benefits, defined contribution plan benefits, retiree
10 medical expense, and employee stock purchase plan. Company Witness Watkins will
11 discuss pension expense and PBOP.

12 **Q. Please describe how labor and labor related expense was calculated.**

13 A. The pro forma salaries and wages expense was calculated on a position-by-position
14 basis, based on 696 full-time positions and 12 temporary summer positions. This
15 means that the 2016 test year labor hours for each employee were analyzed and adjusted
16 to reflect a normal level of labor hours. These hours were then multiplied by the
17 employees’ actual individual 2017 wage rate to determine pro forma labor costs for
18 2017, and inflated using a three-year average salary increase for non-union and
19 contractual wage rates for union employees to determine current test year and future
20 test year costs.

21 Because some labor and labor related costs are capitalized with capital projects and
22 programs, labor and labor related costs are multiplied by an operations and
23 maintenance (“O&M) percentage based on the 2016 ratio of dollars charged to

1 O&M versus capital to derive labor and labor related expense. This eliminates from
2 expenses the labor and labor related costs associated with capital projects and
3 programs, which are appropriately charged to those capital projects.

4 **Q. Please explain how the various components of salaries and wages were calculated.**

5 A. Salaries and wages expense is composed of four components: 1) base pay, 2) overtime
6 expense, 3) wage premiums required by union contract, and 4) annual and long term
7 performance compensation for eligible nonunion employees.

8 Base Pay - In order to calculate the base pay, the wage levels in effect during the 2017
9 period were applied to 2,088 and 2080 hours, for hourly non-union and salaried
10 employees respectively for each full time position and added together. The hours for
11 the 12 temporary summer positions were based on adjusted work hours, each position
12 reflecting .25 hours of a full time employee. Wages for union employees were based
13 on the collective bargaining agreement (“CBA”) wage rates through 2019. If a contract
14 rate has not been negotiated through this date, an hourly rate was calculated using a
15 three-year average increase for each union. Non-union employees’ wage rates were
16 based on actual rates effective at April 1, 2017 to derive the 2017 expense levels. In
17 order to calculate the expense for the current test year and the future test year, the
18 salaries and wages for each non-union position were inflated using a three-year average
19 increase percentage.

20 Overtime - The second component of the labor expense is overtime expense. Overtime
21 was calculated based on a three year average of actual over time dollars from 2014,
22 2015 and 2016. The actual overall labor dollars were divided by the overtime dollars

1 to determine an overtime percentage. This percentage was then applied to the wages
2 for the current test year and future test year to calculate the overtime dollars for each
3 pro forma period respectively.

4 Premium Pay - The third component of the labor expense is the wage rate premiums
5 required by the CBAs for employees who obtain special licenses, who work
6 particular shifts, who operate backhoes, or who work scheduled holidays such as
7 Thanksgiving, Christmas, and the Fourth of July. The premium pay expense is based
8 on the 2016 dollar amount by employee.

9 Performance Pay - The fourth component of labor expense is the annual and long term
10 performance compensation for eligible nonunion employees. Performance pay was
11 calculated on a position by position basis. It was based on each position's target percent
12 for both the Annual Performance Plan ("APP") and Long Term Performance Plan
13 ("LTPP"). The target percent was multiplied by each eligible employee's 2017 pro
14 forma base salary to determine APP and LTPP. The current test year and future test
15 year APP and LTPP were calculated using the same methodology leveraging the current
16 test year and future test year pro forma base salaries. The summary of this adjustment
17 can be can be found on Schedule CAS-13.

18 **Q. Please describe the operating expenses related to payroll tax.**

19 A. Payroll tax expense is directly related to salaries and wages. Two types of taxes are
20 required to be paid in accordance with the Federal Insurance Contributions Act --
21 Old Age Survivors & Disability Insurance ("OASDI," or more commonly "FICA"),
22 and Hospital Insurance (or more commonly "FICA Medicare"). Federal

1 Unemployment Tax (“FUTA”) and State Unemployment Tax (“SUTA”) must also
2 be paid. Pro forma payroll taxes were calculated on a position-by-position basis, using
3 current 2017 tax rates and pro forma wages for the current test year and future test year.
4 The tax rates include 6.2% FICA on up to \$127,200 of wages, 1.45% FICA Medicare
5 on all wages, 0.0% SUTA on the first \$13,000 in wages, and 0.6% FUTA on the
6 first \$7,000 in wages. The summary of this adjustment can be can be found on
7 schedule CAS-13.

8 **Q. Please describe the operating expenses related to group insurance.**

9 A. The adjustment to group insurance expense is composed of two components:
10 PBOP) and other non-PBOP group insurance. I will discuss the non-PBOP group
11 insurance expense. The PBOP expense can be found in the direct testimony of John
12 Watkins.

13 **Q. What is non-PBOP group insurance?**

14 A. Non-PBOP group insurance includes basic life insurance, short- and long-term
15 disability insurance, accidental death and disability (“AD&D”) insurance, and
16 medical, dental, and vision insurance that Missouri-American provides its employees.

17 **Q. How was the pro forma adjustment for the non-PBOP insurance expense
18 calculated?**

19 A. As previously discussed, several types of insurance expense make up this
20 calculation, but they basically comprise two categories: 1) basic life, short- and
21 long-term disability, and AD&D; and 2) medical, dental, and vision insurance.

1 The calculation of the pro forma expense for each of these categories is further
2 described below.

3 Basic life, short- and long-term disability and AD&D. The 2017 pro forma
4 expense for this category was calculated based upon the current 2017 plan rates.
5 The resulting plan costs and contributions rates were used to calculate costs
6 for each employee, according to the insurance stipulations and applying any
7 differences for union and non-union employees. An inflation factor of 2.10%
8 was applied to the 2017 pro forma expense to derive the current test year
9 annualized 2018 expense. An inflation factor of 2.10% was then applied to
10 2018 expense to calculate the future test year expense amounts.

11 Medical, dental, and vision insurance. This category of insurance involves
12 a Company cost net of employee contributions. The costs and contributions
13 vary by plan type (e.g. family, employee, or employee plus spouse). Costs and
14 contributions were calculated on a position-by-position basis, taking into
15 account actual employee plan selections. The 2017 pro forma plan costs and
16 employee contributions were based on current 2017 rates. An inflation factor
17 of 2.10% was applied to the 2017 pro forma expense to derive the current test
18 year annualized expense. An inflation factor of 2.10% was then applied to 2018
19 expense to calculate the future test year expense amounts. The summary of this
20 adjustment can be can be found on Schedule CAS-13.

21 **Q. Please describe the operating expenses related to 401k benefits.**

22 A. Missouri-American incurs 401k expense when it matches employee contributions to
23 401k retirement accounts. The matching amounts are determined by each employee's

1 benefit group or hire date. For employees whose benefit group falls into an “original”
2 category (including union employees hired before 2001 and non-union employees
3 hired before 2006), the Company matches 50% of the first 5% of the employee’s
4 contribution (for a maximum of 2.5%). For the remaining employees, the Company
5 matches 100% of the first 3%, and 50% of the next 2% of the employee’s
6 contributions (for a maximum of 4%). The 2017 pro forma 401k costs were
7 calculated for each employee based on his or her 2017 wages, his or her current
8 employee contribution levels, and the corresponding match for his or her benefit group.
9 The current test year and future test year expense amounts were calculated using the
10 same methodology; however, they were based on the employees’ current test year and
11 future test year pro forma wages. This adjustment is summarized on Schedule CAS –
12 13.

13 **Q. Please describe the adjustment to operating expenses related to the defined**
14 **contribution plan (“DCP”).**

15 A. DCP is a retirement savings program for employees not eligible for the defined
16 benefit pension program. Under the DCP, Missouri-American contributes an amount
17 equal to 5.25% of an employee’s base pay into a retirement account. The 2017 pro
18 forma DCP expense was calculated by multiplying the 2017 pro forma regular time
19 pay of each eligible employee by 5.25%. The current test year and future test year
20 expense amounts were calculated using the same methodology, however they were
21 based on the employees current test year and future test year pro forma wages. A
22 summary of this adjustment is shown on Schedule CAS – 13.

1 **Q. Please describe the adjustment to operating expenses related to retiree medical**
2 **expense.**

3 A. Union employees who are not eligible for PBOP, are entitled to Company-provided
4 retiree medical benefits. Missouri-American has set up a trust (referred to as the
5 Voluntary Employee Benefits Association, or VEBA) to fund this benefit in the
6 amount of \$500 per eligible employee. In an effort to control costs, the Company
7 excludes those employees from PBOP coverage. A summary of this adjustment is
8 shown on Schedule CAS – 13.

9 **Q. Please describe the adjustment to operating expenses related to the employee**
10 **stock purchase plan.**

11 A. The purpose of this adjustment is to annualize the Company's expense associated with
12 the Employee Stock Purchase Plan ("ESPP"). ESPP expense relates to the Company
13 funded 10% discount of American Water stock purchases made through payroll
14 deductions by enrolled employees. The expense was calculated based on the 2017
15 wages for each employee who participates in the plan. The employees 2017 base wage,
16 times their individual contribution amount, applied to the ten percent company discount
17 was used to calculate the 2017 expense. The current test year and future test year
18 expense amounts were calculated using the same methodology, however, they were
19 based on the employees current test year and future test year pro forma wages. The
20 summary of this adjustment can be can be found on Schedule CAS-13.

21 **IV. SUPPORT SERVICES**

22 **Q. What services does MAWC obtain from the Service Company?**

1 A. The services provided by the Service Company include customer service, water quality
2 testing, innovation and environmental stewardship, human resources, communications,
3 information technology, finance, accounting, payroll, tax, legal, engineering, accounts
4 payable, supply chain, and risk management services. The Service Company operates
5 customer service centers in Alton, Illinois and Pensacola, Florida that handle customer
6 calls, billing, and collection activities for MAWC and its public utility affiliates. The
7 customer service centers handle customer inquiries and correspondence, and process
8 service order requests. In addition, the Service Company operates two Field Resource
9 Coordination Centers responsible for tracking and dispatching service orders for our
10 field representatives and distribution crews. The Service Company also operates the
11 Central Laboratory, located in Belleville, Illinois—one of the most advanced water
12 quality laboratories in the United States.

13 **Q. What level of Service Company costs is MAWC seeking in this case?**

14 A. MAWC is seeking recovery of \$30.93 million in Service Company costs for the future
15 test year ending May 31, 2019, which is practically flat when compared to the Service
16 Company costs expected for the current test year (\$30.88 million) and a slight increase
17 over 2016 Service Company costs (\$30.23 million). The requested increase represents
18 only about a two percent (2%) increase over 2016 expenses or about a one-half percent
19 annual increase from 2016 through the future test year. The direct testimony of MAWC
20 witness Patrick Baryenbruch discusses the reasonableness of Service Company costs
21 charged to MAWC. The summary of this adjustment can be can be found on Schedule
22 CAS-13.

1 **II. PRODUCTION COSTS**

2 **Q. Please explain which operating expenses are considered production costs.**

3 A. Production costs are those expenses that vary depending on the amount of water
4 produced by the Company's treatment plants. These costs include fuel and power,
5 chemical, waste disposal, and purchased water.

6 **Q. Please explain the system delivery impact on production costs.**

7 A. System delivery is the amount of treated water that the Company's treatment plants
8 produce. Water sales as well as other factors impact the amount of water produced by
9 the plants, which in turn impacts expenses associated with treating that water. The
10 Company has proposed pro forma revenue adjustments related to declining usage and
11 customer growth as discussed in the direct testimony of Company Witness Gregory P.
12 Roach. Thus, the Company must use the same level of water sales used in its pro forma
13 revenue adjustments to adjust its production related expenses accordingly.

14 **Q. Please describe the fuel and power expense.**

15 A. Fuel and power expense is composed of those costs associated with treating, pumping
16 and delivering water and collecting and treating wastewater. The Company's fuel and
17 power expense is composed of electricity, natural gas and miscellaneous purchased fuel
18 cost. In order to derive the 2017 expense levels the Company made three adjustments
19 to the 2016 base period expense for fuel and power.. The first adjustment removes any
20 accrual amounts from the 2016 base year expense. The second adjustment annualizes
21 the impact of known rate increases, which occurred in 2016 and will occur or have
22 already occurred in 2017. The final adjustment for water recognizes the impact of pro

1 forma system delivery. An inflation factor of 2.10% was applied to the 2017 expense
2 to derive the expenses for the current test year. An inflation factor of 2.10% was then
3 applied to the current test year expense for January to May 2019 to derive the future
4 test year expense levels. The details of this adjustment can be found at Schedule CAS-
5 13.

6 **Q. Please describe the operating expense related to chemicals.**

7 A. The Company uses chemicals to bring chemical and biological contaminants within
8 safe levels, as prescribed by the United States Environmental Protection Agency
9 (“EPA”) in accordance with the Safe Drinking Water Act. Chemicals are also utilized
10 to remove turbidity (cloudiness) of the water and to address any remaining taste and/or
11 odor issues, and for wastewater treatment. Water conditions can vary seasonally or due
12 to other external factors, which impacts chemical usage and expense levels. Examples
13 include drought or flood conditions, fertilizer runoff, water level and temperature. The
14 amount of chemicals utilized by the Company thus varies depending on the season and
15 other external factors. The 2017 expense levels for water were determined by
16 calculating the three-year average usage by chemical. The three-year average chemical
17 usage was then divided by the actual system delivery for the 2016 base year to
18 determine the unit per 1,000 gallons of system delivery. The three-year average cost
19 per pound by chemical is then applied to the 2017 pro forma system delivery to derive
20 the appropriate expense. In order to calculate the current test year and future test year
21 expense levels an inflation factor of 2.10% was applied the pro forma system delivery
22 for the respective periods. The 2017 expense levels for sewer were determined by
23 calculating the 2016 base year chemical usage to the 2017 cost per chemical. The cost

1 was then inflated by 2.10% for the current test period and future test period. The details
2 of this adjustment can be found at Schedule CAS-13.

3 **Q. Please describe the operating expense related to waste disposal.**

4 A. The Company incurs waste disposal costs as a result of the need to properly dispose of
5 sludge and other by-products resulting from water and wastewater treatment. Missouri-
6 American treats waste disposal in some areas while in others, specifically related to
7 wastewater, the company leverages a third party for treatment. Sludge removal and
8 lagoon cleaning for MAWC occurs on a cycle ranging from 5 to 600 months. The
9 cleaning schedule is based on the amount of waste and size of lagoon, consistent with
10 EPA standards. Some lagoons are cleaned on an annual basis while others may only
11 be cleaned every 240 months, with the average cleaning cycle running 24 months. The
12 expense for waste disposal includes those charges incurred in 2016 and accrued
13 expense for future scheduled cleanings in waste disposal. The accruals plus other
14 monthly expensed waste disposal charges recorded by Missouri-American is
15 representative of the total waste disposal expense. The accounting department using
16 information provided by MAWC Operations Managers/Supervisors for each respective
17 district records these accruals. The accrual amounts are reviewed on a quarterly basis
18 and updated if necessary. The expense levels for the current and future test period were
19 calculated based on current accrual amounts by location with inflation factor applied
20 for the respective periods. The purpose of this adjustment is to annualize the
21 Company's expense related to waste disposal. The details of this adjustment can be
22 found at Schedule CAS-13.

23 **Q. Please describe the operating expense related to purchased water.**

1 A. The purchased water expense includes the costs for purchasing water from other
2 utilities. Contract purchase requirements and cost per thousand gallons are used to
3 derive the expense. The purpose of this adjustment is to annualize the costs incurred
4 to purchase water from outside sources. In order to calculate the expense, the Company
5 used the 2016 per book system delivery by month, multiplied times the applicable rate,
6 plus applicable taxes. Any miscoded items were then removed from the expense levels.
7 Rate increases for each purchased water district were reviewed to determine average
8 increase over a three-year period and applied by month to the applicable rate. A three-
9 year average consumption was calculated for each purchased water district and applied
10 to the calculated rate. This provided the current test year annualized 2018 expense
11 levels. The future test year expense levels were calculated in the same manner, using
12 the three-year average increase applied to the three-year average consumption. The
13 details of this adjustment can be found at Schedule CAS-13.

14 **VI. OTHER OPERATING EXPENSES**

15 **Q. Please describe the operating expenses related to rents.**

16 A. Missouri-American incurs expense for rental costs associated with copy machines,
17 other miscellaneous items, and two office locations- one at 727 Craig Rd St Louis
18 Missouri, and one located at 1050 Fox Chase Industrial Court in Arnold Missouri. In
19 order to calculate the appropriate expense levels for known office lease terms, the
20 Company took the 2016 actual expenses and adjusted for changes in lease terms to
21 derive the 2017 expense levels. In order to calculate the current test year expense for
22 the remaining leases, the 2017 copier and miscellaneous lease expense levels were
23 inflated by 2.10% and added to the building lease expense, for an annualized 2018

1 period. The future test year expense was calculated by applying an inflation factor of
2 2.10% to the copier and miscellaneous lease expense and added to the building lease
3 expense for the January through May 2019 expense levels. The summary of this
4 adjustment can be found on Schedule CAS-13.

5 **Q. Please describe the operating expenses related to transportation.**

6 A. Transportation expense includes transportation, operation and maintenance, and fuel
7 costs. The Company first calculated its annualized 2017 pro forma transportation lease
8 expense based on changes in leased vehicle and equipment levels as of January 2017,
9 and twelve month average fuel rates. The maintenance expense was calculated based
10 on the 2016 test period expense increased by the inflation factor of 2.00%. The O&M
11 percentage was applied to the expense to obtain the O&M expense portion of the
12 adjustment. The current test year pro forma expense was calculated by taking the 2017
13 lease expense, inflating specific maintenance items and gasoline expense by an
14 inflation factor of 2.10% for the full 12 month period. The future test year expense was
15 calculated by applying an inflation factor of 2.10% to the January through May 2019
16 expense levels for specific maintenance items and gasoline added to the lease expense.
17 The summary of this adjustment can be can be found on Schedule CAS-13.

18 **Q. Please describe the operating expenses related to postage and customer
19 accounting.**

20 A. The operating expense for postage and customer accounting is inclusive of expenses
21 related to customer invoice mailings. In addition, it includes items from customer
22 accounting expense such as; bill inserts, collection notices, lock box fees for payment
23 collection, water quality reports, and customer communications etc. The pro forma

1 adjustment for postage expense was calculated by applying 2017 postal rates from the
2 latest rate filing by the United States Postal Service to the number of actual mailings
3 for 2016, adjusted for any acquisitions and projected growth for 2017. The current test
4 year was calculated by adjusting the 2017 mailings for growth and acquisitions then
5 applied to the 2017 postage rate inflated at 2.00%. The future test year was calculated
6 by adjusting the 2018 projected mailings adjusted for growth, acquisitions, and the St
7 Louis County quarterly to monthly billing conversion, then applied to the 2018 inflated
8 postage rate inflated again for the period of January through May of 2019 with an
9 inflation factor of 2.00%. The remaining customer accounting expenses were
10 calculated leveraging an inflation factor of 2.00%, 2.10% and 2.10% for 2017, 2018
11 and 2019 respectively for the current test year and a partial years inflation factor for the
12 future test year. The summary of this adjustment can be found on Schedule CAS-13.

13 **Q. Please describe the operating expenses related to miscellaneous expense.**

14 A. The operating expense described as miscellaneous expense includes expenses for
15 charitable contributions, penalties and membership dues, lobbying, relocation
16 expenses, office power, heating and oil, as well as other miscellaneous expenses; such
17 as telephone, cell phone, shipping, uniforms, and customer education expenses. The
18 miscellaneous expense adjustment then removes expenses for charitable contributions,
19 penalties and membership dues, lobbying and relocation expense. The details of this
20 adjustment can be found at Schedule CAS-13.

21 **Q. Please describe the operating expenses related to contract services.**

22 A. The contracted services expense includes costs associated with landscaping, Missouri
23 one call, accounting, audit and legal fees that are performed by a contracted third party.

1 In order to calculate the appropriate expense levels the Company took the 2016 actual
2 expenses and adjusted for acquisitions, and removal of the tank painting tracker
3 expense dollars to derive the 2017 expense levels. In order to calculate the current test
4 year expense, the 2017 levels were inflated by 2.10% for an annualized 2018 period.
5 The future test year expense was calculated by applying an inflation factor of 2.10% to
6 the January through May 2019 expense levels. The details of this adjustment can be
7 found at Schedule CAS-13.

8 **Q. Please describe the operating expenses related to maintenance supplies and**
9 **services.**

10 A. The operating expense associated with maintenance supplies and services are those
11 expenses associated with maintenance cost for the general operation of the business,
12 hydrant painting expense, and finally main break expense for St Louis County.

13 **Q. Please discuss the maintenance supplies and services expense associated with**
14 **hydrant painting.**

15 A. The first part of the expense is the maintenance cost for the general operation of the
16 business and hydrant painting. In order to calculate the appropriate expense levels, the
17 Company took the 2016 actual expenses and adjusted for acquisitions, miscoded
18 invoices and anticipated hydrant painting cost to derive the 2017 expense levels. In
19 order to calculate the current test year, the 2017 levels were adjusted for any
20 acquisitions, additional hydrant painting expense, and inflated by 2.10% for an
21 annualized 2018 period. The future test year expense was calculated by adjusting for
22 any acquisitions, additional hydrant painting expense, and applying an inflation factor
23 of 2.10% to the January through May 2019 expense levels. Please see the direct

1 testimony of Andrew Clarkson for additional detail regarding hydrant painting.

2 **Q. Please discuss the maintenance supplies and services expense associated with main**
3 **breaks.**

4 A. The Company calculated an adjustment for main break expense associated with breaks
5 that occur in St Louis County. The purpose of this adjustment is to annualize main
6 break expense to a normalized, pro forma level based on a review of historical main
7 breaks and the cost to repair the breaks in St Louis County. In order to calculate the
8 appropriate expense levels, the Company took a three-year average count of main
9 breaks and expense from 2014, 2015, and 2016 actual expenses. The three-year
10 average expense was then applied to a 2.00% inflation factor to derive the annualized
11 2017 expense levels. In order to calculate the current test year expense, the 2017 levels
12 were inflated by 2.10% for an annualized 2018 period. The future test year expense
13 was calculated by applying an inflation factor of 2.10% to the January through May
14 2019 expense levels. The details of this adjustment can be found at Schedule CAS-13.
15 Please see the direct testimony of Andrew Clarkson for additional detail regarding main
16 breaks.

17 **Q. Please describe the operating expenses related to tank painting.**

18 A. The tank painting expense includes costs associated with painting the interior and
19 exterior of system water storage tanks. In order to calculate the appropriate expense
20 levels, the Company determined the projected cost of painting specific tanks for the
21 2017, 2018, and 2019 periods, using 2016 as the base period for expense. The
22 Company then used these projected expense levels to determine the level of expense
23 for the current test year as well as the future test year. The current test year was

1 calculated by using 7 months of the projected 2017 expense and 5 months of the
2 projected 2018 expense, plus amounts remaining from the deferred tank-painting
3 tracker. The future test year was calculated using 7 months of the projected 2018
4 expense levels, and 5 months of the projected 2019 expense levels, plus amounts
5 remaining from the deferred tank painting tracker. The 2019 expense level includes a
6 reduction to the tracker amortization of \$148,668. This represents a 3-year
7 amortization of \$445,990 dollar tank painting tracker liability, which is also reflected
8 in the CAS-3 schedule. The details of this adjustment can be found at Schedule CAS-
9 13. Please see the direct testimony of Andrew Clarkson for additional detail regarding
10 tank painting.

11 **Q. Please describe how the Company's insurance other than group costs are**
12 **determined.**

13 A. Missouri-American incurs costs related to several types of insurance, including Auto
14 Liability, General Liability, Worker's Compensation, and Property. The insurance
15 costs are referred to as insurance other than group ("IOTG"). The Company's General
16 Liability, Auto Liability and Workers Compensation premium is based upon a
17 combination of loss experience (50%) and exposure (50% estimated annual revenue
18 and payroll). Exposure for Auto Liability uses estimated annual revenue, payroll and
19 number of vehicles. The loss experience is based upon a 5-year average of historical
20 loss experience. The 5-year average is used to smooth out losses to the extent that
21 MAWC suffers an anomalous year of claims experience. This is consistent with the
22 commercial insurance market underwriting practice.

23 **Q. Please describe the IOTG pro forma adjustments to operating expenses.**

1 A. The majority of the Company's IOTG premiums renew on January 1 of each year
2 (Directors & Officers Liability insurance renews in April each year). Development of
3 the pro forma expense begins with the annual premiums owed as of early 2017, which
4 are \$465,458 higher than the premiums in 2016. The 2017 level of IOTG expense is
5 adjusted first to arrive at the annualized expense level for the 12 months ending of May
6 31, 2018, and then to arrive at a forecast expense for the twelve months ending May
7 31, 2019. The first adjustment to these premiums is an annual inflation factor of 2.1%,
8 which is applied to policies, which expire before May 31, 2018. Next, the pro forma
9 capitalized labor percentage was multiplied by the new Worker's Compensation
10 premium, to reduce the expense. After this, an adjustment is made to increase IOTG
11 due to various acquisitions. The 2017 level was adjusted to remove capitalized credits
12 for certain insurance premiums not capitalized by other MAWC affiliates. These
13 credits totaled \$447,351 in 2016. Please also see Schedule CAS-13 for the detailed
14 calculation.

15

16 **Q. Please describe the operating expenses related to uncollectible expense.**

17 A. Uncollectible expense are those dollars associated with bad debt. In prior cases, the
18 Company has calculated the uncollectable expense by applying a 3-year average of net-
19 charge offs to billed water and sewer revenue for a twelve-month period. However,
20 recent trends in uncollectible percentage of billed revenue have shown a steady decline
21 year over year. In 2014, uncollectibles represented 1.69% of total billed water and
22 sewer revenue. In 2015, uncollectibles represented 1.55% of total billed water and
23 sewer revenue. Finally, in 2016, uncollectibles represented 1.05% of total billed water
24 and sewer revenue. As such, the Company believes that the uncollectible percentage

1 will not reach the 3-year average of 1.43%, rather the trend supports a reduced number
2 of 0.75% net charge offs to water and sewer revenue in this filing. The uncollectible
3 expense amount is calculated by taking the 0.75% uncollectible percentage, applied to
4 the total Company projected revenues for the period. The same methodology was used
5 for the 2018, and 2019 expense levels using the projected revenues for each respective
6 period. The summary of this adjustment can be found on Schedule CAS-13.

7 **Q. Please describe the adjustment to operating expenses related to PSC Assessment.**

8 A. The purpose of this adjustment is to annualize the PSC Assessment fee. The pro forma
9 amount is based on the current PSC Assessment ratio of 1.091415180% for fiscal year
10 beginning July 2016. The annual PSC Ratio of 1.091415180% is applied to the May
11 2018 Twelve months Pro Forma Present rate Revenue to obtain the May 2019 PSC
12 expense. The summary of this adjustment is found on Schedule CAS-13.

13 **Q. Does this conclude your direct testimony?**

14 A. Yes, it does.